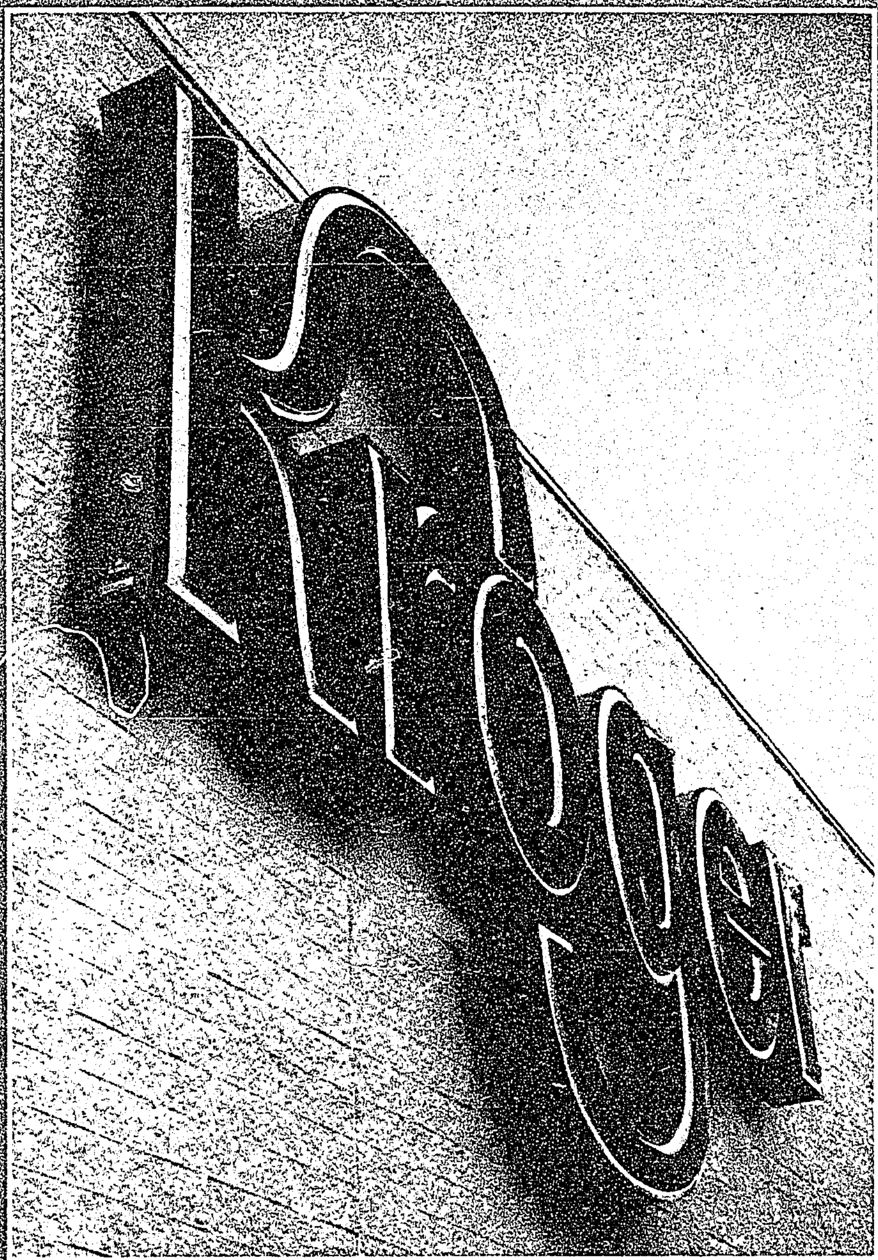
The Kroger Company Annual Report -- 1980
America's Corporate Foundation; 1980; ProQuest Historical Annual Reports
pg. 0_1

The Kroger Co.
Annual Report 1980



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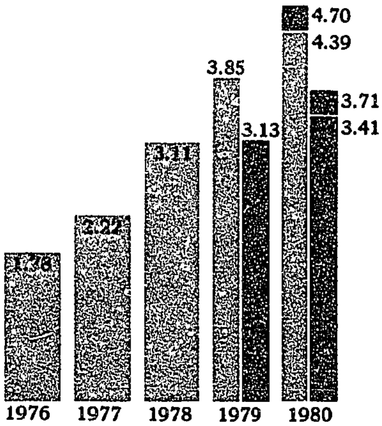
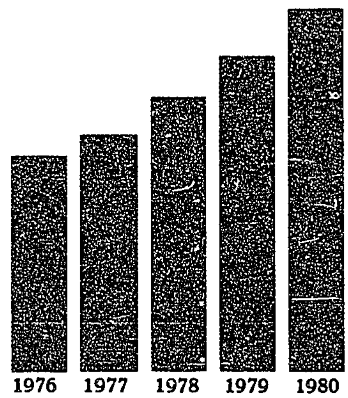
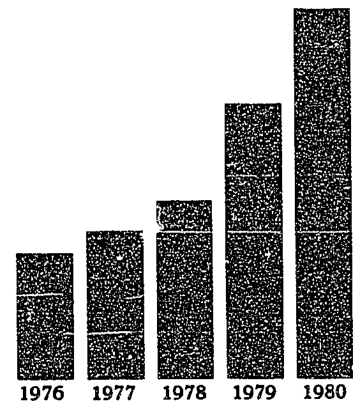
Earnings Per Share



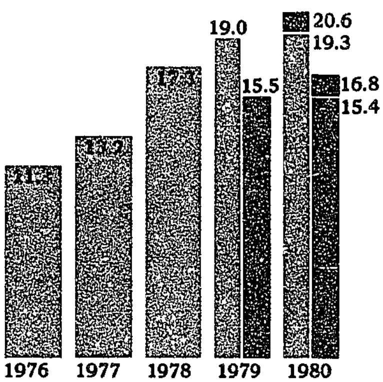
Sales
(Billions)



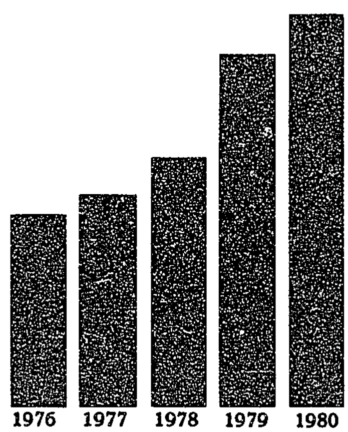
Capital Expenditures
(Millions)



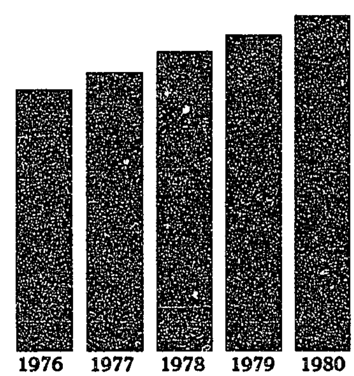
Return on Beginning Shareowners' Equity



Dividends Per Share



Food Store Square Footage
(Millions of Square Feet)



FIFO
FIFO Continuing Operations
LIFO
LIFO Continuing Operations

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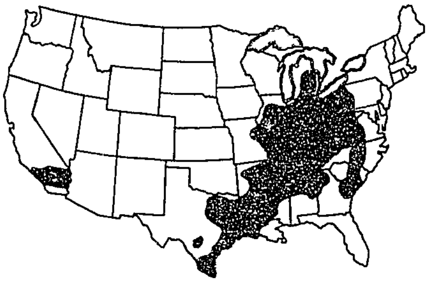
Food Stores

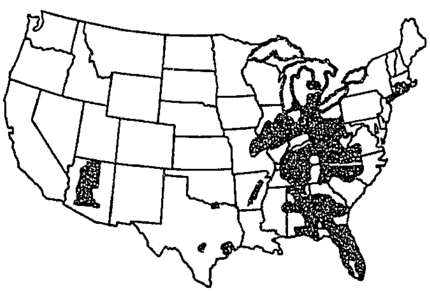


THE KROGER CO. is the fifth largest retailing company in the United States as ranked by total sales. The Company's largest operation is Kroger Food Stores, the second largest retail food chain, with 1245 food stores in 21 states at the end of 1980. More than 90% of retail food store space is new or remodeled in the 1972-80 period. Most of these improved facilities are in the 25-45,000 square foot superstore category, and about 40% of the new stores planned for 1981 will be 40,000-square-feet-and-up combination stores. Modern Kroger food stores offer a variety of specialty departments, such as a delicatessen, fresh bakery, floral and cheese shops, service meat and fresh seafood, service fragrance and cosmetics, expanded non-foods, and in some, a pharmacy and a sit-down restaurant. Nearly two-thirds of the 110 new food stores to be opened in 1981 will be located in the Sun Belt.

Processing Facilities

Kroger also processes food for sale in its food stores, a tradition which began before the turn of the century. The Company operates eight bakeries and eight dairies in addition to a cheese plant, egg grading and packing plants, a peanut butter plant, a candy plant, a pet foods plant, a delicatessen kitchen, a pharmaceutical plant and a general processing plant where such products as coffee, tea, preserves, salad dressings, spices, nuts and other items are processed. A new dairy in Tennessee to serve the growing number of stores in the South and a 145,000 square foot bakery that will produce hearth-baked breads and rolls and basic doughs for producing a wide variety of baked goods in Kroger in-store bakeries will begin production in 1981. Other private label products are prepared for sale in Kroger stores by leading food processors throughout the country.

SupeRx Drug Stores



SupeRx Drug Stores, with 514 drug stores in 21 states at the end of 1980, is one of the nation's largest drug store chains. Although SupeRx operates a majority of its drug stores in states where Kroger Food Stores are located, drug stores also are located in Arizona, Connecticut, Florida, New Jersey and New York. SupeRx has embarked on a major modernization program which is designed to restore and reinforce their drug store and health care image — strengthening those departments traditionally associated with drug stores (such as pharmacy, cosmetics, optical centers, health food centers and greeting cards). At the end of 1980, SupeRx had built new or converted 75 stores to the new SupeRx II concept. In 1981, plans call for 50 new and 40 remodeled drug stores.

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The Kroger Floral Shoppe

A recent article about Kroger's floral shoppes in the *Cincinnati Post* was headlined: Sweet Smell of Success in Kroger's Floral Shoppes.

From a few [illegible] in the early '70s, Kroger's floral business has blossomed into a full-fledged in-store floral shoppe—offering a wide variety of blooming and foliage plants, cut fresh flowers and arrangements, and dried and silk flowers. They'll be pleased to blend a bouquet, a corsage or an arrangement to order! At the end of [illegible], there were 280 floral shoppes in Kroger stores. This will grow to [illegible] by the end of this year.

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Financial Highlights

	1980	1979	Change
Sales	$10.3 billion	$9.0 billion	+ 14.3%
LIFO Results			
Earnings from continuing operations	$102.8 million	$85.7 million	+ 19.9%
Net Earnings	$94.4 million	$85.7 million	+ 10.1%
Per Common Share			
Earnings from continuing operations	$3.71	$3.13	+ $.58
Net Earnings	$3.41	$3.13	+ $.28
FIFO Results			
Earnings from continuing operations	$130.0 million	$105.5 million	+ 23.2%
Net Earnings	$121.6 million	$105.5 million	+ 15.3%
Per Common Share			
Earnings from continuing operations	$4.70	$3.85	+ $.85
Net Earnings	$4.39	$3.85	+ $.54
Dividends Paid	$38.8 million	$34.5 million	+ 12.3%
Per Common Share	$1.40	$1.26	+ $.14
Real Estate Data			
Food Stores			
Opened	118	88	
Remodeled	49	91	
Total Area (sq. ft.)	34.5 million	32.5 million	
Drug Stores			
Opened and Acquired	42	38	
Remodeled	27	2	
Total Area (sq. ft.)	5.8 million	5.7 million	

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To Our Fellow Shareowners:

The Kroger Co. in 1980 was able to utilize the strengths created over the past several years to achieve another satisfactory year.

Annual earnings from continuing operations were up 20% despite a $13.8 million increase in pre-tax LIFO charges and two major work stoppages (West Virginia in the first quarter and Houston in the fourth quarter). We were able to cope with such factors as the midwestern recession as well as other economic problems. We showed a sales increase above the inflation rate, maintained our building program, and increased the dividend for our shareowners.

In 1980 (53 weeks):

- Sales of $10.317 billion were up 14.3% over 1979 (52 weeks).
- Earnings from continuing operations were $102.8 million on a LIFO basis, compared to $85.7 million in 1979.
- Earnings per share from continuing operations were $3.71, compared to 1979 per share earnings of $3.13.
- The quarterly dividend was increased from 34¢ to 38¢ per share, effective with the December 1 payment. This was the seventh increase in the past five years, more than doubling the quarterly dividend from 72¢ on an annual basis to its present $1.52.

Net earnings for 1980 of $94.4 million were reduced by provision of $8.4 million for an estimated loss resulting from our decision to dispose of our interest in the amusement park business. Per share earnings (LIFO) were $3.41 after the 30¢ non-recurring loss.

The events of 1980 reinforce our confidence that the kinds of stores and the one-stop shopping presentation that we are giving the consumer can perform effectively in almost any economic circumstance. They also demonstrated the talent and the continuing ability of the Kroger team to function effectively and to produce results.

Our Kroger food stores, which are planned to serve as broad a group of the consuming public as possible, combine aggressively competitive prices with other wanted factors such as quality, broad product variety and friendly service. This is particularly visible in the perishable departments, such as produce, where the differences that make Kroger stand out from our competition are most evident.

Our service specialty departments, such as delicatessens, in-store bakeries, cheese, floral and now sit-down restaurants, are steadily attracting growing sales at a rate twice as fast as the rest of the store. These broader customer offerings help improve profitability because of the better margins compared to traditional supermarket departments.

By the end of 1982, some 80% of our stores will contain a variety of these service specialty departments.

Non-foods general merchandise, which in our new 42,000 square foot combination stores may account for a third or more of store space, also is contributing to our ability to be price competitive and yet be able to improve earnings.

Capital Expenditures

Capital expenditures in 1980 totaled $239 million.

During 1980, we opened 118 new food stores — a third of them in the 42,000 square foot category with service specialty departments and substantially expanded non-foods. We remodeled 49 stores, many including substantial enlargements.

More than half of our total food store development in the year was in the fast-growing Sun Belt, although we are at the same time protecting our business in other parts of the country by keeping our facilities up-to-date and modern. We closed 86 stores during the year and sold our food business in western and northern Michigan (21 stores) which had been unprofitable.

This development brought our total food store square footage to 34.5 million at the end of the year, up 2.1 million net square feet during 1980. At the end of the year, we operated 1245 food stores.

Kroger Food Processing

One of the key areas in which Kroger is able to give significant value and variety to budget-conscious shoppers is our extensive line of Kroger private label products, some two-thirds of which are processed in our own plants.

Our manufacturing facilities continue to expand to meet the growing customer demand for these fine products. A new dairy is scheduled to open soon in Tennessee to serve the growing number of stores in the South and Southeast. We also are now operating an ice cream novelties plant in Georgia, as well as a pet foods plant and a distribution center for manufactured products, both in Tennessee.

Initial production from our unique new bakery in Kentucky is expected to begin late in 1981. The 145,000 square foot bakery will provide hearth-baked breads and rolls as well as basic doughs for producing a wide variety of baked goods in Kroger in-store bakeries.

During the year, we sold our Cincinnati sausage business, which had at best been only marginally profitable. The new operators continue to supply Kroger stores with private label wieners and luncheon meats.

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Amusement Park Business

Kroger has agreed in principle to sell its interest in Kings Dominion amusement park to Taft Broadcasting Company in exchange for one million shares of Taft Series B preferred stock, with a par value of $20 per share. The preferred shares are redeemable over a 12-year period and provide for dividend and principal payments totaling $2.5 million annually. Taft and Kroger, through a joint venture, Family Leisure Centers, have been partners in Kings Dominion, which has been operated by Taft. The sale will free capital for investment in our basic food and drug store business.

SupeRx Drug Stores

As expected, earnings of the SupeRx drug store division contributed only modestly to 1980 profits, continuing to reflect the expense of converting the drug stores to the new SupeRx II health care concept.

SupeRx sales in 1980 (53 weeks) totaled $635 million, an increase of 12% from sales of $567 million in 1979 (52 weeks). Operating profit of $9.8 million dropped $3.0 million from 1979 operating profit of $12.8 million.

While we were dissatisfied with the 1980 SupeRx results, we have a strong and growing conviction that the path we are taking with our drug stores is correct. The sales results in the stores which have been built new or converted to the SupeRx II concept are encouraging. Although most of the 75 SupeRx II stores in operation at year end were opened in the second half of 1980, sales are already ahead of sales in conventional stores — a response similar to the early Kroger superstores. Consumer research of the early SupeRx II stores is very strong in support of this type of health-related drug store.

During 1980, SupeRx opened 42 stores, remodeled 27 into the new concept and closed 32, ending the year with 514 stores.

This has been a year of intense activity for SupeRx. There is an adverse profit impact during the rebuilding period, particularly as product lines are changed, inventories of discontinued items are liquidated, stores are modernized and the men and women who will run them are trained. This is, however, an investment that we are confident will be rewarding to shareowners as we accomplish the fulfillment of our plans.

Looking Ahead – 1981

During the year of 1981, we will continue to build our storing and marketing strategy on a firm foundation of experience and research.

Our capital spending is expected to be in the neighborhood of $250 million. We plan to open 110 new and 62 remodeled food stores. Most will be in the 35,000 to 42,000 square foot range.

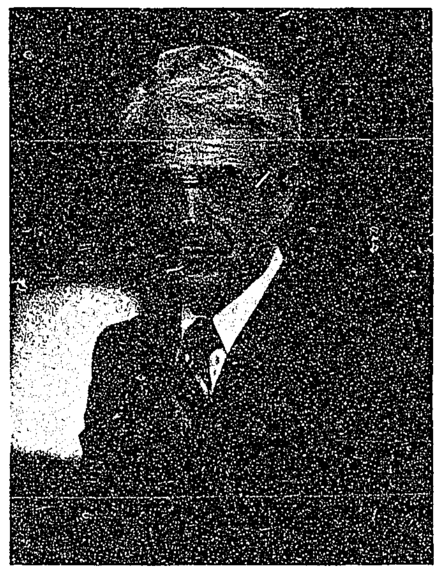
A total of 50 new and 40 remodeled drug stores are planned for the year as we continue to convert stores to the SupeRx II concept.

Approximately $60 million of our capital spending will go to equip our manufacturing division to keep pace with the growing needs of our food and drug business for fine Kroger-made products.

In January, 1981, we announced that agreement has been reached with The Daiei, Inc., Japan's largest food and general merchandise retailer, to explore opportunities for joint ventures in the future. At present, activities are largely exploratory, although our food processing division will in 1981 begin to export food items for sale in Daiei and affiliated stores in Japan and Hawaii. Daiei in turn will assist Kroger in the procurement of selected merchandise from the Orient for sale in our food and drug stores.

Kroger enters 1981 with stronger momentum than a year ago. This will be a year of significant challenges — not the least of which is the strong rate of food inflation being predicted because of widespread, often worldwide, shortages in some basic commodities. At Kroger, we believe our private label capabilities and the broad range of choices we offer the shopper give us the ability to satisfy customers in the predicted kind of environment.

It also gives us reasonable assurance that we can produce sales and earnings for our shareowners that will compare favorably with both the food industry and with other businesses.



Sincerely,

Lyle Everingham

Chairman of the Board
and President

March 25, 1981

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The store and an ever-growing constituency of satisfied customers is the key to the business success of The Kroger Co. Our principal objective is to be a profitable, performance-proven leader in food/drug retailing and manufacturing, with recognition coming from our customers, our shareowners, our employees and our industry.

The business of The Kroger Co. is the sale of food and drug products through 1700-plus retail stores in 26 states in the Middle West and South. Our corporate strategy is linked to the growing preference of consumers for one-stop shopping.

As customer behavior changes, our business behavior changes with it. With gasoline prices up, shopping trips are more carefully planned. Two-income families have become the norm rather than the exception. Families are smaller, the average age of the population is rising and many social values have changed. These and other trends in society produce continuing changes in life style. All impact our business.

At Kroger, we recognize and respond to these changes—and through this response, we build a better business.

Our Business Philosophy

To track the changing needs of shoppers, we are constantly taking the pulse of our customers. They direct us. In our stores, we will capture and retain their loyalty by serving them more effectively:

— We listen to shoppers, through comprehensive and probing consumer research (we will conduct 200,000 customer interviews in 1981), and we will be guided by what they tell us;

— We attract shoppers by assuring them everyday low prices, not by using games or gimmicks which do not add value to what they buy;

— We offer shoppers a totality of values, so that no matter what their income or life style, they will always find what they want and need at prices they can afford and at quality levels they demand; our goal is to become *the* store to shop because we satisfy more of the customer's needs than any other store or combination of stores;

— We will continue to provide shoppers with a pleasant experience each time they visit us, in stores that are clean, modern, well-stocked and staffed by friendly and helpful employees;

— We will satisfy our shoppers' food and drug needs so well that they will become loyal and regular customers.

Our Strategy

In the next five years, our business behavior will be marked by these characteristics:

We will invest primarily in regions demonstrating increased population and expanded consumer purchasing power. We will move with the people and do business where they live.

We will keep our balance sheet strong and our financial ratios supportive of favorable ratings by the investment community. We will carry out our financing on an anticipatory basis, dedicated to the protection of our "A" credit rating.

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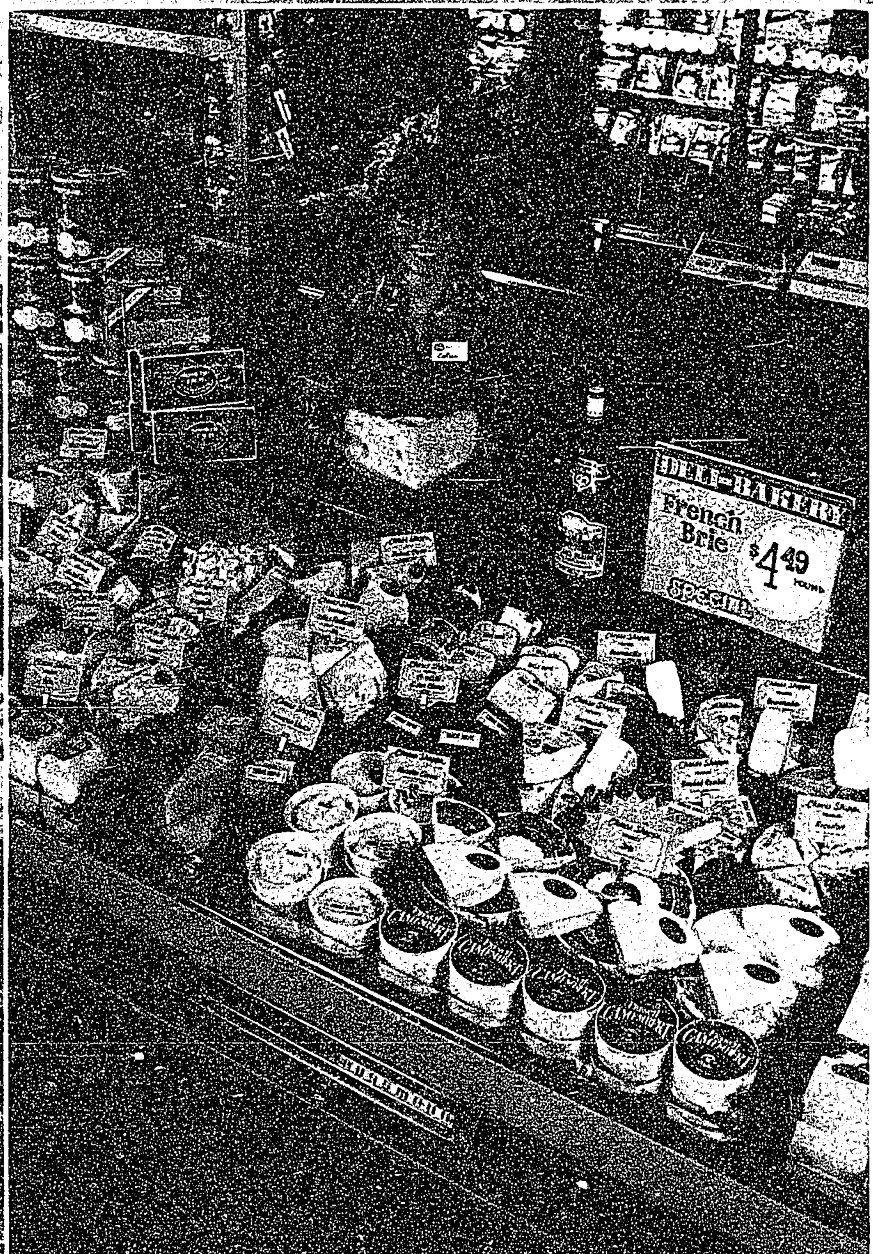
The Kroger Cheese Shop



French Brie and Danish Havarti are becoming a regular part of the shopping list for a growing number of [illegible] customers in the [illegible] cheese shops in Kroger stores. [illegible] approximately 130 additional [illegible] shops are planned for 198[illegible].

Sampling is a regular part of shopping the Kroger cheese shop [illegible] around [illegible] are among [illegible]. In addition to counter customers, they'll also make up cheese balls and party trays for cheese-loving partying.

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We will remain committed to staying contemporary. Our resources, both physical and human, will be kept modern and vibrant. We will build new food and drug stores and remodel existing ones regularly. We will update our processing plants consistently. We will enable our people to acquire the skills and experiences needed to stay abreast of a fast-paced business in a constantly-changing world.

We will conduct a disciplined reappraisal of unproductive investments each year. Those which have been operating for some time but have remained underproductive will be redeployed in a timely and rational fashion to areas where they can contribute to company earnings. We will not be reluctant to abandon existing areas and mature facilities which no longer contribute to corporate growth.

We will compare our total results against the best performing companies in our business. At the minimum, we will achieve a return on equity which matches the average of this peer group as we move consistently toward the higher end of the range. Our objective is to produce a return on equity which will trend upward in consistent fashion. Executive incentive compensation will be based, in part, on attainment of these goals.

We will achieve a share of market which allows us to serve shoppers better and provide the necessary support service economically. We will consistently increase the number of major markets in which our customers rank us as superior merchants.

We will share the end product of our progress with the owners of our business by increasing our dividend regularly, consistent with earnings growth. In balancing our obligation to shareowners with our financing needs, we will maintain a dividend payout ratio in the range of 35-45% of the previous year's earnings (calculated on a FIFO basis).

Our Challenges

Currently, we face challenges to our management skills:
— Operating costs in our industry, pushed by a surge in energy prices and unabated labor cost increases, continue to rise.
— This cost push puts pressure on gross profit margins.

We have been attentive to these trends, and have met them resourcefully. Still, we are not yet comfortable with our record of coping with them. The challenges are not beyond our abilities, but they continue to test our management skills.

Some illustrations:

Rising Energy Costs. We have dramatically reduced the consumption of energy, both electricity and oil and gas, through the use of conservation techniques and equipment. And yet, the cost of each unit of energy continues to rise more rapidly than we have offset by using fewer units.

More dramatic steps now must be considered, such as moving away from a restricted number of large plants and warehouses to a larger number of smaller facilities in order to control fuel consumption and transportation cost more effectively.

Rising Labor Costs. We have negotiated some labor contracts with more favorable cost structures and fewer work restrictions. And yet, our annual labor bill continues to rise faster than we have offset it with productivity gains. Accelerated installation of new laborsaving equipment appears mandated, such as the expanded use of front-end scanning in our stores and higher levels of automation in all our facilities.

Additionally, the computer has created a flow of information which measurably improves the quality of the management decision-making process as we seek to cope with these challenges. We intend to continue our investment in and effective use of this information flow so that we remain in the forefront of computer-assisted management.

Pressure on Margins. Daily, we search for a way out of the dilemma created by the constant need to remain very price competitive on the one hand and the consistent rise in operating costs on the other. Our ingenuity is further tested as we seek to enhance retail gross margins. We believe we have found a strategy which can be effective, not only in the near-term but in the long-term as well. This strategy consists of three compatible components:
— Providing for shoppers a wide variety of everyday household food and drug products which are sensitive to price competition and low margin in nature;

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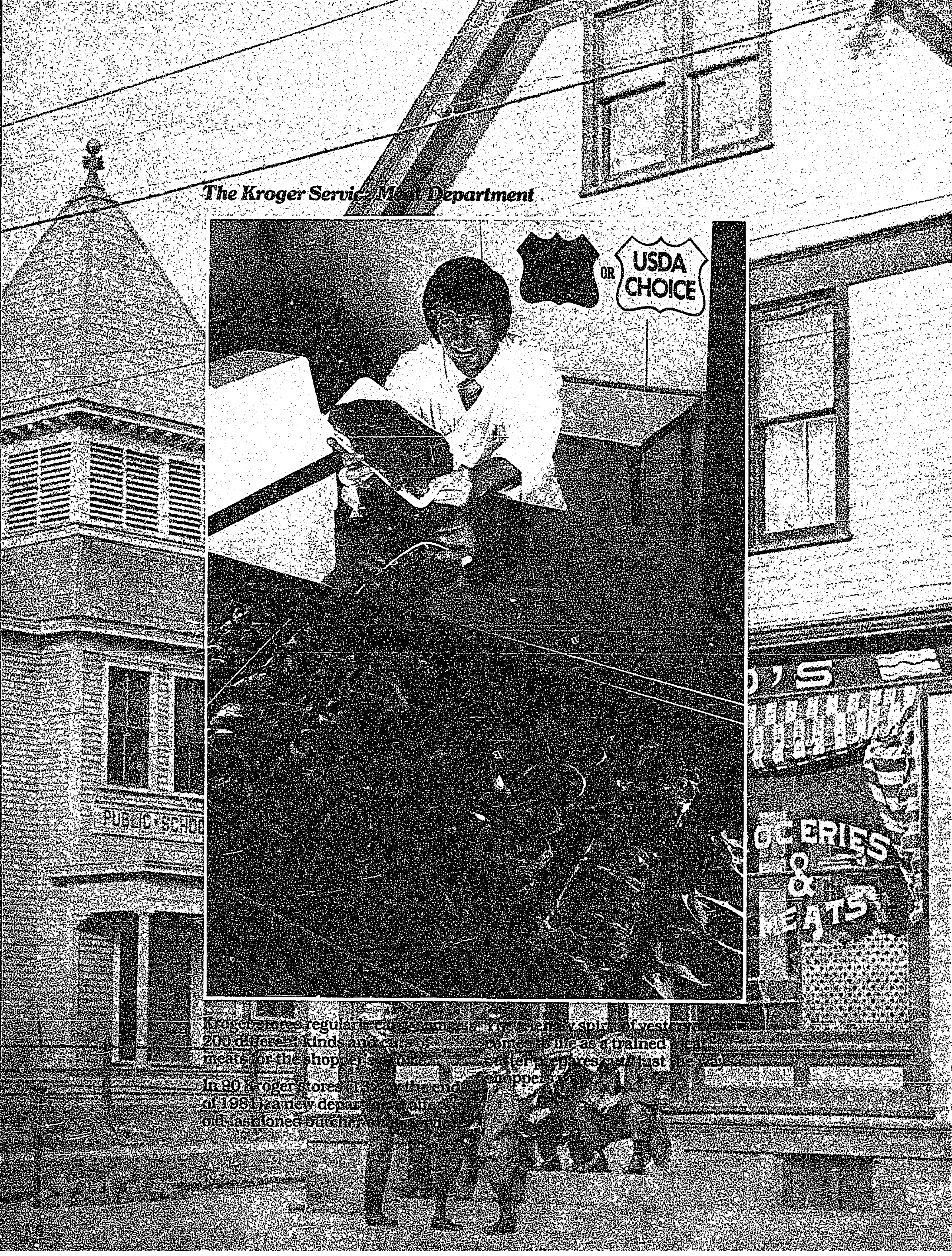
The Kroger Servi[illegible] M[illegible] Department



Kroger stores regularly carry some [illegible] 200 different kinds and cuts of meats for the shopper's choice.

In 90 Kroger stores (1[illegible] by the end of 1981), a new department [illegible] old-fashioned butcher [illegible]

The [illegible] spirit of yesterday comes to life as a trained meat cutter prepares cuts just the way shoppers [illegible]

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— Serving the huge market created by our high volume stores and effectively marketing frequently-used products made in our own efficient manufacturing plants;
— Providing an array of specialty departments which are less susceptible to price sensitivity but provide a customer value and carry higher gross margins.

These higher-margin specialty departments—delicatessens, bakeries, cheese shops, floral shoppes, snack bars, pharmacies, cosmetics and fragrance boutiques, service meat and fish departments—provide us with a way in which to stay competitive on basic pantry groceries and enrich our total gross margins at the same time.

A carefully selected assortment of general merchandise further enhances margins while increasing our ability to attract the one-stop shopper. Our non-food merchandise lines will stress frequently-used, fast-turn household items—as contrasted to fashion goods. Still, we will expand this area of our business only as our competence and confidence grows with experience, in recognition of the differences between food and non-food merchandising.

Drug Stores. We must improve upon the record of our SupeRx drug stores. Earnings have been inconsistent. Our investment in this enterprise warrants better results.

Our plan for SupeRx is sound: To capitalize upon a credible health care image in order to rebuild the business, producing sustained earnings improvements as we go. Execution of the plan, on the other hand, will not be easily accomplished and will require considerable patience, unswerving dedication and discipline—and time, perhaps as much as several years.

The SupeRx strategy is founded on these main points:
— Developing of a product and service department mix which serves the health and personal care needs of customers (pharmacy, health and beauty aids, health foods center, cosmetics and fragrances, optical shops);
— Creating a reputation with customers for consistently offering these products and services at everyday low prices;
— Converting from a direct store delivery distribution system to a warehouse delivered system;
— Concentrating of store building efforts in selected major markets where increased storing can produce a more efficient operation and enhance profitability;
— Strengthening our professional pharmacy service as a major business asset favored by increasing numbers of customers.

SupeRx stores are being remodeled and built new to the health care emphasis. In-store disciplines are improving. A new distribution center is maturing and beginning to contribute to higher efficiencies. The management team has been reconstituted and is applying its retailing experience with increasing effectiveness.

Deficiencies take time to remedy and cost money in the near-term. The early results of the new and remodeled SupeRx II stores are encouraging and give us confidence that our direction and thrust are correct.

Our Strengths

Our record in dealing effectively with these challenges will have a significant influence on our ability to succeed totally. We remain confident our current strengths will enable us to be up to the task. We believe these proven strengths to be:
— Retail stores that are young in age, modern in design and decor, and contemporary in their appeal to customers;
— Dedication to research in all its forms in order to determine what kind of stores to build and where to build them;
— Demonstrated excellence in the merchandising of the perishable products so influential in the customer's choice of where to shop;
— Strategically located, highly efficient manufacturing facilities providing a wide variety of quality label products uniquely available to our customers;
— Marketing strategies based on everyday low prices the customer can depend on consistently in the search for values;
— An executive team which combines youth and experience in a blend of talents pledged to the attainment of aggressive goals.

While we expect the mainstream of our business in the foreseeable future to remain as it is today (food/drug retailing and manufacturing), we will not be reluctant to examine—on a selective basis—opportunities to enter new ventures which could capitalize on our strengths.

But we will resist the temptation to reach beyond our ability to manage or to divert our attention from the primary activities of the enterprise. Our primary focus will continue to be our retail businesses and our responsibility to keep them a consistent, dependable source of corporate profitability.

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The Kroger Fresh Bakery

A crusty [illegible] bread, a [illegible] [illegible] birthday [illegible] they're all stock in trade [illegible] 702

When the new Bowling Gree[illegible] bakery is completed, it will [illegible] the basic doughs that talented [illegible]

[illegible]

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Q. The need to remain price-competitive and the steady rise in operating costs have combined to create a dilemma for companies as they strive to increase gross margins. Kroger has said that its overall profit margins will be improved by the addition of higher-margin service specialty departments. Can you be more specific about how these departments can aid margins?

A. Accompanying the rise in operating costs and intensified price competitiveness in the food industry is the need to improve retail gross margins to accommodate these needs—both to absorb operating cost increases and to assist earnings growth. But this must be accomplished while maintaining low, competitive prices, since this is one of the key ingredients of attracting shoppers.

There are some obvious correlations between our service specialty departments in particular and the growing number of shoppers who are more sophisticated, with less time and more money, and who are single or with smaller families. These departments also help maintain and improve gross margins.

In our stores, we can balance out the lower markup on basic foods with what is for us a higher markup for specialty departments and non-foods—even though our price may be lower than traditional outlets such as department stores, florists or fast-food outlets. Sales in our service specialty departments are growing at a rate twice as fast as in the rest of the store.

We have tended to think of the specialty departments as "extras" which contribute only peripherally to total store sales. Today these specialty departments are approaching the same percent of store sales as produce, and at nearly twice the gross margin of the overall store.

More than 70% of our food stores now contain a variety of these specialty departments, growing to 80% of our food stores by the end of 1982. In the 1980's, these departments will become an even more integral part of our store concept, with the emphasis developing in response to consumer research and shopper needs.

Q. Consumer research has been a key to Kroger's retailing success. How has this research helped Kroger to run a better business, and what are your plans for 1981?

A. Since the beginning of our superstore program, we have used consumer research to help us pinpoint the strengths and weaknesses of Kroger and of our competition. We use it to fine-tune our stores and our merchandising to keep pace with and to anticipate changing consumer needs.

The most visible evidence of how listening to consumers has played a conspicuous part in Kroger's merchandising vitality is our produce department.

Most fresh fruits and vegetables used to be sold enclosed in cellophane. When we took the product out of the package... insisted on only top quality... expanded the variety (among our most popular items today are Oriental vegetables and tropical fruits)... and put someone in the department to answer questions and weigh purchases—sales increased significantly.

The various service specialty departments pictured in this Annual Report are in Kroger stores today because consumer research showed that shoppers wanted and needed them.

In the past two years, we have talked personally with a quarter million consumers. In 1981, we will conduct approximately 200,000 consumer interviews. And we'll respond to what they tell us.

Other kinds of research are an important part of planning as well. Real estate research provides the information to make educated decisions on where stores are located and where new stores should be. Manufacturing research and development gives us the ability to operate the finest processing facilities in the nation, and also is opening exciting vistas for future directions. Research in other senses, such as continuous monitoring of legislative and regulatory trends that will affect Kroger, becomes of key importance as government exerts growing influence on how our business is operated.

Q. Kroger during the 1970's maintained its store modernization program despite industry problems and government disincentives for investment. With 100-125 new food stores and 40-50 drug stores a year scheduled for the next several years, along with appropriate manufacturing and support facilities, Kroger's capital needs in the 1980's will grow. What will be your capital needs in the next several years and how do you plan to finance capital expenditures?

A. Most of our capital requirements will come from operating cash flow and LIFO tax deductions, but we intend to continue our financing on an anticipatory basis. One of the reasons Kroger was able to maintain its building program in the past decade has been the fact that we anticipated financing needs as much as two years.

The LIFO accounting method provided $23.2 million in cash in 1980 and is expected to provide about $150 million for the years 1981-85.

We are beginning to see signs that the traditional source of investment funds utilized by our store landlords may be less accessible. Thus far the investors who build Kroger stores and lease them to us have been able to obtain the necessary financing. Should this situation change in the future, we may have to consider alternatives,

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including financing store buildings ourselves. Whatever is necessary, we believe that modern facilities are essential to retail success.

Because of the money situation, which is a universal problem, 1982 and 1983 could represent a challenge in maintaining our level of store openings. Storing plans for 1981 are established and our building program well under way. Capital expenditures are expected to accelerate from about $250 million this year on a gradual basis to $330 million by 1985.

Q. ***Kroger's manufacturing division has primarily served the food stores. Will there be a change in direction for this part of the business in the next decade?***

A. The major thrust of our manufacturing division will continue to be geared to the growing needs and opportunities offered through our Kroger food stores. Supplying fine Kroger-made products to our retail stores will always be the main area of effort of our manufacturing division.

However, we expect to increase our sales of manufactured products to outside customers when capacities permit and profitable opportunities exist. For example, in 1981 we will begin shipping non-perishable products, such as coffee, preserves and dry mix products, to the Daiei stores in Japan and Hawaii. Also, we plan to expand our existing and growing base of outside domestic customers.

We also plan to move selectively into profitable new lines now being produced by others and sold under a Kroger label in our food stores — such as our pet foods plant in Tennessee, our Kentucky bakery which will produce hearth-baked goods and frozen doughs for store bake-offs, and possibly other lines such as home cleaning products, pasta products or expanded lines of snacks or beverages.

Also, we are looking at distribution and procurement patterns as transportation costs rise. As our geographic emphasis shifts southward, it makes good economic sense to locate support facilities in strategic locations to serve our stores most economically and efficiently. We will be moving toward a larger number of smaller, specialized plants which are located closer to the source of supply.

For example, our Georgia peanut butter plant is in the heart of the peanut-growing area and we have opened a second distribution center for manufactured products in Tennessee to serve the Sun Belt. Extracts are now being prepared and packaged at our pharmaceutical plant, where capability for such work already existed, rather than replace the previous extract facilities which had become outdated. At the same time, this helps us to utilize the pharmaceutical plant more fully.

Q. ***With approximately two-thirds of food store operating costs going for labor, what is Kroger doing to try to control the rising labor bill?***

A. During the 1980's, we will continue to strive to achieve with the union officials who represent our employees an understanding of our mutual dependence on the success of the Company. We must learn to recognize and respect each other's problems ... to be open, honest and candid ... and working together, to develop labor contracts that will fairly meet the needs of employees, yet give organized companies such as Kroger the ability to compete on a comparable basis with non-union food retailers.

There have been some discouraging situations, such as union insistence on a contract that enlarged an already-huge differential in hourly labor cost with competition in western Michigan — resulting in sale of our food business in that area. But we see signs that enlightened union leadership recognizes that increased job opportunities are more important than temporary wage/fringe gains.

And Kroger has been adding jobs. In the past five years, the total number of Kroger employees has grown 50% — from 83,374 to 124,642 well-paid men and women.

Q. ***You state that Kroger's annual labor bill continues to rise faster than you have been able to offset it with productivity gains and that "accelerated installation of new laborsaving equipment appears mandated." Use of scanner checkout systems in the supermarket has been heralded as a major development in assisting productivity in the food industry. What are Kroger's plans and will this investment accomplish what it is designed to do?***

A. At the end of 1980, a total of 192 of our food stores were equipped with these new checkout systems, which both assist productivity and offer improved customer service. An additional 150 stores will be equipped with scanning equipment in 1981. We have updated our installation schedule by a year because of the scanner's demonstrated value.

After several years of testing of different systems, we are now more than ever convinced that scanners are an essential investment and that there are a number of ways that the system provides savings and improves our operation. There is some productivity improvement, as well as better inventory control, less out-of-stock, and enhanced customer service.

In addition, the system *(which provides an itemized receipt tape, an optical viewer as the product is rung up, and shelf tags which also show the unit price)* eliminates the need to pricemark 4,500,000 individual items a year per store. We have been selectively using shelf pricing instead of individual item pricing because of the further savings it represents.

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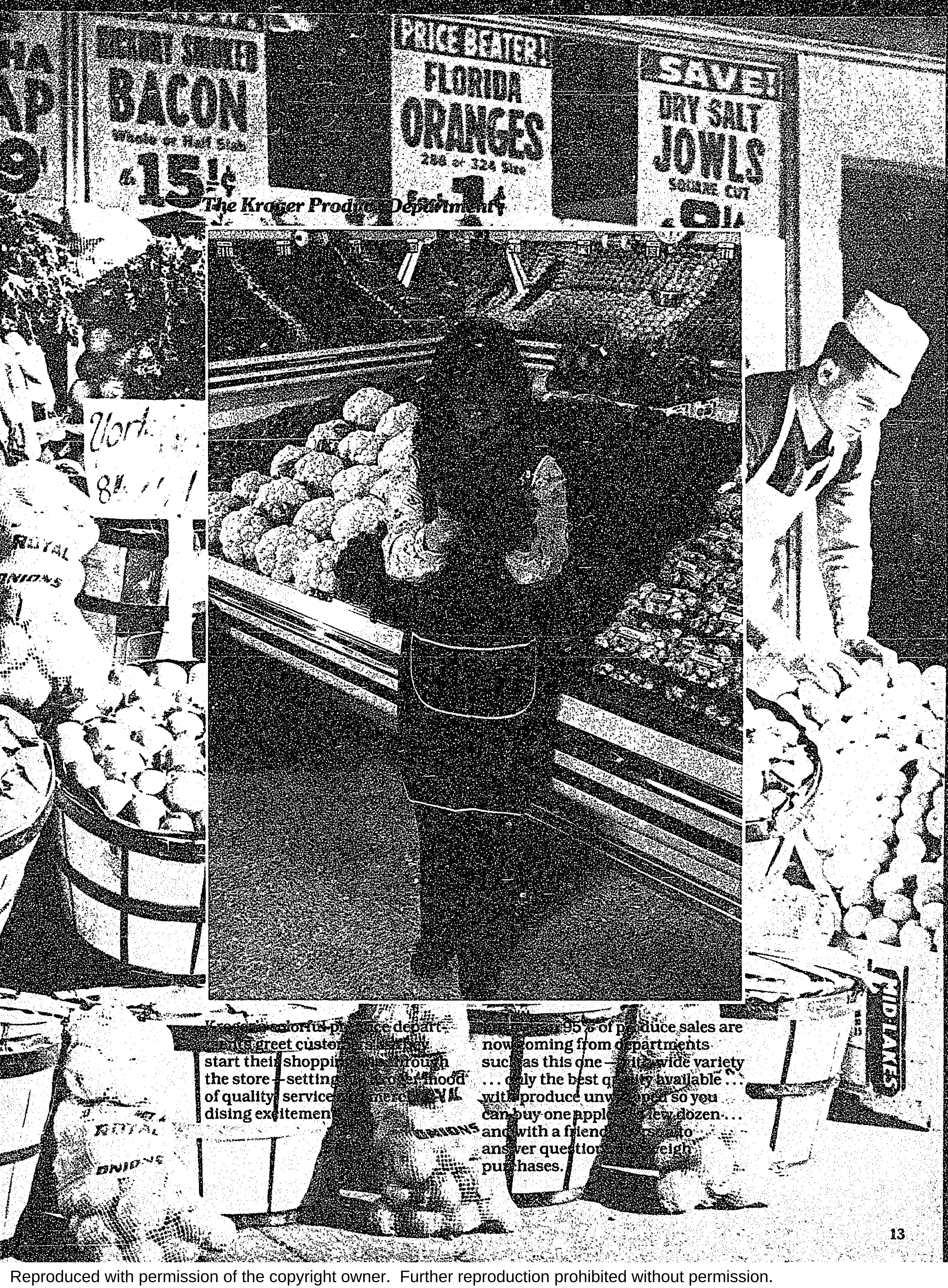

The Kroger Produce Department

Kroger's colorful produce departments greet customers as they start their shopping trip through the store — setting the overall mood of quality, service and merchandising excitement.

[illegible] 95% of produce sales are now coming from departments such as this one — with a wide variety . . . only the best quality available . . . with produce unwrapped so you can buy one apple or a few dozen . . . and with a friendly person to answer questions and weigh purchases.

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This analysis of Company operations encompasses the years 1978, 1979 and 1980 and should be considered in conjunction with the Consolidated Statement of Earnings, page 19; Operating Results by Segments of Business, page 18; The Ten Year Summary, page 34; and the Consolidated Statement of Changes in Financial Position, page 23.

Liquidity & Capital Resources

The Company's capital expenditures and dividends over the past three years required funds totalling $628.1 million of which $551.1 million came from operations. The balance of required funds came primarily from long-term financing arrangements. Increased indebtedness in 1980 resulted primarily from the issuance of $50.0 million additional long-term debentures and $12.4 million in industrial revenue bonds. Over the past three years, shareowners' equity improved $181.4 million or 37.0% while net long-term debt increased $29.3 million or 12.2%.

Sources of Funds in Millions

	Operations		Other		Total	
	Amt.	Chg.	Amt.	Chg.	Amt.	Chg.
1980	$217.7	+25.7%	$92.7	+134.9%	$310.4	+45.9%
1979	173.3	+ 8.2%	39.4	+ 6.6%	212.7	+ 7.9%
1978	160.1	+22.4%	37.0	+ 23.0%	197.1	+22.5%

Working capital changes and LIFO effects are summarized as follows:

	1980	1979	1978
	(in millions)		
Net decrease in working capital (LIFO)	$20.7	$41.6	$4.9
LIFO charge	50.4	36.7	0
Net increase (decrease) in working capital plus LIFO charge	$29.7	($4.9)	($4.9)

Capital expenditures in 1980 were $239.1 million, having increased from $176.9 million in 1979 and $114.5 million in 1978, which represented 67.4% of total uses of working capital.

Summary of Retail Expansion

	Food			Drug		
	#of Stores		Total Sq. Footage	#of Stores		Total Sq. Footage
	New	Remodeled		New	Remodeled	
1980	118	49	34.5 Million	42	27	5.8 Million
1979	88	91	32.5 Million	38	2	5.7 Million
1978	104	58	30.7 Million	7	4	5.6 Million

In 1981 capital spending is projected to exceed $250 million with plans for 160 new retail stores, 102 remodeled stores, and substantial investments in manufacturing facilities.

The Company anticipates that funds to support its expansion program will come primarily from operations with additional funding from long-term debt and industrial revenue bonds. The Company's strategy is to utilize long-term financing, with the timing, principal amount and form dependent on prevailing securities market and general economic conditions.

Long-term debt and obligations under capital leases as a percent of capitalization (Long-Term Debt and Obligations under Capital Leases + Shareowners' Equity) was 36.5% at year end, as compared to 35.7% at year end 1979, and 37.2% at year end 1978. This ratio is expected to remain in the 35% to 40% range.

As of January 3, 1981, the Company had unused lines of credit of $130.6 million with banks, of which $100.0 million was a revolving credit agreement expiring in May, 1983, which is convertible to a four year term loan any time prior to the expiration date. In 1980, short-term borrowings averaged $8.9 million as compared to $3.9 million in 1979 and no significant short-term borrowings in 1978.

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Improved control of inventory levels has been a key factor in relieving pressure for short-term financing. Average (FIFO) inventory turns in 1980 improved to 9.5 as compared to 9.2 in 1979 and 9.4 in 1978.

Company ownership of properties has increased during the past year. This trend will continue and probably accelerate in view of present financial markets and possible changes in federal tax laws affecting depreciation rates.

Results of Operations

Consolidated sales in 1980 (53 weeks) of $10.3 billion increased 14.3% over 1979. Food store sales in 1980 of $9.7 billion were 14.4% improved over 1979. Drug store sales of $635.0 million were 12.0% over 1979.

Consolidated Sales *(in millions)*

	1980		1979		1978	
	Amt.	Chg.	Amt.	Chg.	Amt.	Chg.
Food Stores	$ 9,682	+14.4%	$8,462	+15.8%	$7,306	+17.4%
Drug Stores	635	+12.0%	567	+ 8.6%	522	− .9%
Total	$10,317	+14.3%	$9,029	+15.3%	$7,828	+16.0%

Food store sales in 1980 were affected by a 9.0% increase in prices and a 5.1% increase in tonnage. The latter was favorably impacted by increased customer transactions and expanded food store square footage.

Drug store sales in 1980 were impacted by an approximate 9 to 9.5% increase in prices and a 2.5% increase in customer transactions. Drug store square footage increased slightly from 1979.

Merchandise costs, including warehousing and transportation, as a percent of sales remained relatively constant during the past three years. The 1980 LIFO charge to inventories of $50.4 million unfavorably impacted merchandise costs for the food store segment of business, compared to the 1979 LIFO charge of $36.7 million. There was no LIFO charge in 1978.

LIFO Effect on Merchandise Costs as a Percent of Sales *(in millions)*

	1980		1979		1978	
	Amt.	% Sales	Amt.	% Sales	Amt.	% Sales
Mdse. Costs (FIFO)	$7,962	77.2	$7,019	77.7	$6,084	77.7
LIFO Charge	50	.5	37	.4		
Mdse. Costs (LIFO)	$8,012	77.7	$7,056	78.1	$6,084	77.7

Food store merchandise costs, including warehousing and transportation, as a percent of sales was 78.2% in 1980 as compared to 78.8% in 1979. The decline reflects a change in product mix of food stores as the number of specialty departments increased and the non-foods/general merchandise departments were expanded.

Drug store merchandise costs, including warehousing and transportation, as a percent of sales were 69.4% in 1980 as compared to 68.1% in 1979. Significant factors impacting this category were a 13.5% increase in merchandise costs and increased warehousing and transportation expenses of $1.4 million (+50%) over 1979, the latter due primarily to expenses connected with the new warehouse facility in Melbourne, Florida.

Operating, general and administrative expenses as a percent of sales increased to 18.4% in 1980 from 18.0% in 1979 and 18.0% in 1978. The increase in 1980 was principally the result of higher employee related costs and higher energy costs. Employee related costs increased 18.4% from 1979 and energy costs increased 23.9% from 1979.

	Wages & Salaries In Millions		Fringe Costs In Millions		Energy Costs In Millions	
	Amt.	Chg.	Amt.	Chg.	Amt.	Chg.
Food	$1,036.9	+16.9%	$312.4	+28.8%	$116.2	+24.2%
Drug	92.6	+14.0%	22.9	+17.1%	9.3	+20.3%
Total	$1,129.5	+15.8%	$335.3	+28.0%	$125.5	+23.9%

Food business operating profit (before taxes based on income and unallocated expenses) was $194.3 million (LIFO) which compared favorably to $166.7 million (LIFO) in 1979 and to $168.9 million (FIFO)in 1978. The LIFO charge to food business inventories adversely impacted operating profits by $50.4 million in 1980 and $36.7 million in 1979.

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Operating profit (before taxes based on income and unallocated expenses) of drug stores of $9.8 million declined from $12.8 million in 1979 and $22.6 million in 1978. The decline in 1979 from 1978 was due primarily to increased advertising and inventory expenditures that failed to produce anticipated sales while other operating expenses increased. The decline in 1980 operating profits reflects the abnormal expenses connected with the store building program throughout the year, particularly as product lines were changed, discontinued inventories liquidated, stores remodeled, and personnel trained. Although profits were and will continue to be adversely affected during the rebuilding period, improvement is expected as stores mature.

Net Earnings

Earnings from continuing operations were $102.8 million in 1980 as compared to $85.7 million in 1979 and $84.6 million in 1978. Earnings from continuing operations in 1980 were reduced by a provision of $8.4 million for an estimated loss resulting from the Company's decision to dispose of its interest in the amusement park business (see footnote page 25). Non-recurring events that favorably impacted earnings were capital gains totaling $8.2 million resulting from the sale of 21 Western Michigan stores, distribution facilities, and a sausage plant. Two major work stoppages (West Virginia and Houston) had an unfavorable impact on annual earnings.

Earnings from continuing operations on a FIFO basis in 1980 were $130.0 million as compared to $105.5 million in 1979 and $84.6 million in 1978. On a comparable basis 1980 earnings from continuing operations increased 23.2% over 1979.

The high rate of inflation experienced in the United States in recent years has impacted the Company's reported earnings, shareowners' equity and other financial data. The Company has not attempted to measure that impact by traditional accounting methods. However, an estimation and evaluation of the effect of inflation, as defined by Statement of Financial Accounting Standards No. 33, Financial Reporting and Changing Prices, follows on page 31.

Management's Responsibility for Financial Reporting

The consolidated financial statements of The Kroger Co. and Consolidated Subsidiary Companies as well as other financial information contained in this report were prepared by management which is responsible for their integrity and completeness. These statements were prepared in conformity with generally accepted accounting principles and necessarily include some amounts that are based on management's best estimates and judgments.

The Company has over the years maintained a system of internal accounting controls to provide reasonable assurance that Company assets are adequately protected, and transactions are executed in accordance with management's authorizations and are reflected accurately in the Company's books and records as a basis for the reliable preparation of the financial statements. The system of controls includes careful selection and training of financial management personnel, clearly defined limits of authority and division of responsibility, the dissemination of detailed formal accounting and business policies and procedures and an extensive program of internal audit examinations to monitor the effectiveness of the control system. The Company has distributed to key employees its policy requiring high moral, ethical and legal standards in the conduct of its business.

Coopers & Lybrand, certified public accountants, have examined the consolidated financial statements in accordance with generally accepted auditing standards. Their report on the consolidated financial statements appears on page 30.

The Board of Directors acting through its Audit Committee, which is comprised entirely of outside directors, oversees the fulfillment by management of its responsibilities in the preparation of financial statements and financial control. The Committee recommends the selection of the Company's certified public accountants, reviews the scope, training, and costs of the internal and external audit programs and meets formally at least twice per year with the internal and external auditors, providing them direct free access at these and other times.

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Quarterly Data

Quarterly sales, merchandise costs (including warehousing and transportation), net earnings and net earnings per share for 1980 and 1979 were as follows:

Quarter	Sales In Millions 1980	Sales In Millions 1979	Merchandise Costs In Millions 1980	Merchandise Costs In Millions 1979	Net Earnings In Millions 1980	Net Earnings In Millions 1979	Net Earnings Per Share 1980	Net Earnings Per Share 1979
1st (12 Weeks)	$ 2,189	$1,927	$1,710	$1,504	$12.4	$15.5	$.45	$.57
2nd (12 Weeks)	2,289	2,061	1,767	1,607	27.0	22.7	.98	.83
3rd (16 Weeks)	3,121	2,791	2,425	2,187	25.4	19.8	.91	.72
4th (13 Weeks in 1980) (12 Weeks in 1979)	2,718	2,250	2,110	1,758	29.6(a)	27.7	1.07(a)	1.01
Total	$10,317	$9,029	$8,012	$7,056	$94.4(a)	$85.7	$3.41(a)	$3.13

(a) Net Earnings were reduced by a provision of $8.4 million or 30¢ per share for an estimated loss resulting from the Company's decision to dispose of its interest in the amusement park business.

The LIFO method of valuing inventories reduced net earnings as follows:

(In thousands of dollars except per share figures)

	1980 Net Earnings	1980 Net Earnings Per Share	1979 Net Earnings	1979 Net Earnings Per Share
1st Quarter	$ 4,561	$ .16	$ 4,226	$ .15
2nd Quarter	6,547	.24	4,531	.17
3rd Quarter	8,970	.33	6,156	.22
4th Quarter	7,147	.25	4,882	.18
	$27,225	$ .98	$19,795	$ .72

Common Stock Price Range

	1980 High	1980 Low	1979 High	1979 Low
1st Quarter	19	15	21⅛	17½
2nd Quarter	20¼	14	20½	18¾
3rd Quarter	23¾	19½	27	19⅜
4th Quarter	22⅜	19⅞	24¾	17⅝

Main trading market — New York Stock Exchange (Symbol KR)

Number of shareowners at year end
1980 — 38,190
1979 — 37,849

Dividends Paid Per Share

Date Paid	1980	1979
March 1	$ .34	$ .29
June 1	.34	.29
September 1	.34	.34
December 1	.38	.34
	$1.40	$1.26

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The Company's segments of business information for the years 1978 through 1980 were:

	1980 (53 Weeks)	1979 (52 Weeks)	1978 (52 Weeks)
	(in millions of dollars)		
Sales:			
Food Business	$ 9,682	$ 8,462	$ 7,306
Drug Stores	635	567	522
Total	$ 10,317	$ 9,029	$ 7,828
Operating Profit:			
Food Business	$ 194.3	$ 166.7(a)	$ 168.9
Drug Stores	9.8	12.8	22.6
	$ 204.1	$ 179.5	$ 191.5
Unallocated Expenses:			
Corporate expenses, net	$ 5.8	$ 3.6	$ 8.2
Interest expense	35.7	29.4	30.0
	$ 41.5	$ 33.0	$ 38.2
Earnings from continuing operations before taxes based on income	$ 162.6	$ 146.5(a)	$ 153.3
Taxes based on income	59.8	60.8	68.7
Earnings from continuing operations	$ 102.8	$ 85.7(a)	$ 84.6
Identifiable Assets:			
Food Business	$1,633.8	$1,376.2	$1,284.9
Drug Stores	208.6	204.5	162.4
Other unallocated	155.1	212.6	205.7
	$1,997.5	$1,793.3	$1,653.0
Capital Expenditures:			
Food Business	$ 224.5	$ 155.4	$ 108.0
Drug Stores	$ 13.2	$ 10.9	$ 4.2
Depreciation and Amortization:			
Food Business	$ 80.0	$ 66.0	$ 60.6
Drug Stores	$ 4.3	$ 3.5	$ 3.2

(a) Food Business Operating Profit was reduced by $36.7 million and earnings from continuing operations were reduced by $19.8 million as a result of the change from the FIFO method to the LIFO method of valuing grocery inventories.

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Consolidated Statement of Earnings

Years Ended January 3, 1981, December 29, 1979 and December 30, 1978 (In thousands of dollars, except per share amounts).

	1980 (53 Weeks)	1979 (52 Weeks)	1978 (52 Weeks)
Sales	$10,316,741	$ 9,029,315	$ 7,828,071
Costs and Expenses:			
Merchandise costs, including warehousing and transportation	$ 8,011,872	$ 7,056,035	$ 6,084,005
Operating, general and administrative expenses	1,901,178	1,625,974	1,407,960
Rent	130,632	112,527	99,785
Depreciation and amortization	86,166	71,574	65,179
Dividend and interest income	(11,403)	(12,688)	(12,097)
Interest expense, including interest on obligations under capital leases	35,736	29,385	29,983
Total	$10,154,181	$ 8,882,807	$ 7,674,815
Earnings from continuing operations before taxes based on income	$ 162,560	$ 146,508	$ 153,256
Taxes based on income	59,774	60,787	68,660
Earnings from continuing operations	$ 102,786	$ 85,721	$ 84,596
Operations to be discontinued:			
Loss from operations	$ (548)		
Estimated loss on disposal	(7,852)		
	$ (8,400)		
Net earnings	$ 94,386	$ 85,721	$ 84,596
Average number of shares of common stock outstanding	27,681,273	27,407,201	27,208,058
Earnings (loss) per share of common stock:			
From continuing operations	$3.71	$3.13	$3.11
From operations to be discontinued:			
Loss from operations	(.02)		
Estimated loss on disposal	(.28)		
Net earnings	$3.41	$3.13	$3.11

The accompanying notes are an integral part of the consolidated financial statements.

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Consolidated Balance Sheet

(In thousands of dollars)

Assets	Jan. 3, 1981	Dec. 29, 1979
Current Assets		
Cash and temporary cash investments	$ 92,872	$ 75,234
Receivables	105,624	79,884
Inventories:		
FIFO cost	862,341	817,355
Less LIFO reserve	(87,073)	(36,657)
	775,268	780,698
Store and general supplies	10,562	9,105
Prepaid and other current assets	61,471	33,068
Total current assets	$1,045,797	$ 977,989
Investments		
Marketable investment securities	$ 17,476	$ 19,515
Investments in operations to be discontinued	23,873	45,492
Other investments	7,581	6,831
Total investments	$ 48,930	$ 71,838
Property, Plant and Equipment		
Land	$ 32,811	$ 28,059
Buildings and land improvements	168,662	149,573
Equipment	783,754	650,035
Leaseholds and leasehold improvements	237,321	205,107
Leased property under capital leases	152,866	137,270
	$1,375,414	$1,170,044
Allowance for depreciation and amortization	(490,797)	(444,824)
Property, plant and equipment, net	$ 884,617	$ 725,220
Excess of cost of investments in consolidated subsidiaries over equities in net assets	$ 18,201	$ 18,224
Total Assets	$1,997,545	$1,793,271

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Liabilities

	Jan. 3, 1981	Dec. 29, 1979
Current Liabilities		
Current portion of long-term debt	$ 6,080	$ 3,152
Current portion of obligations under capital leases	3,741	3,057
Notes payable	14,700	17,025
Accounts payable	504,334	467,298
Accrued expenses:		
Salaries and wages	110,188	96,707
Taxes, other than income taxes	104,527	79,295
Other	45,114	43,553
Accrued income taxes	30,190	20,272
Total current liabilities	$ 818,874	$ 730,359
Other Liabilities		
Long-term debt	$ 268,146	$ 233,937
Obligations under capital leases	117,819	106,055
Deferred federal income taxes	95,353	84,677
Employees' benefit fund	25,987	26,915
Total other liabilities	$ 507,305	$ 451,584
Total Liabilities	$1,326,179	$1,181,943
Shareowners' Equity		
Common capital stock, par $1, at stated value		
Authorized: 50,000,000 shares		
Issued: 1980—28,142,872;		
1979—28,038,187	$ 96,748	$ 94,749
Accumulated earnings	590,429	534,811
	$ 687,177	$ 629,560
Common stock in treasury, at cost—1980—370,401 shares		
1979—426,660 shares	(5,672)	(6,534)
Net unrealized loss on marketable equity securities	(10,139)	(11,698)
Total Shareowners' Equity	$ 671,366	$ 611,328
Total Liabilities and Shareowners' Equity	$1,997,545	$1,793,271

The accompanying notes are an integral part of the consolidated financial statements.

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Consolidated Statement of Shareowners' Equity

Years Ended January 3, 1981, December 29, 1979 and December 30, 1978 (In thousands of dollars)

	Common Stock						
	Issued		Treasury Stock		Accumulated Earnings	Valuation Allowance	Total Shareowners' Equity
	Shares	Amount	Shares	Amount			
Balance, December 31, 1977	27,704,252	$90,661	(580,454)	$(9,658)	$423,236	$(14,267)	$489,972
Net earnings for the year					84,596		84,596
Dividends on common stock, $.89 per share					(24,218)		(24,218)
Exercise of stock options	137,854	1,237					1,237
Decrease in net unrealized loss on marketable equity securities						2,920	2,920
Balance, December 30, 1978	27,842,106	$91,898	(580,454)	$(9,658)	$483,614	$(11,347)	$554,507
Net earnings for the year					85,721		85,721
Dividends on common stock, $1.26 per share					(34,524)		(34,524)
Exercise of stock options	196,081	1,952					1,952
Increase in net unrealized loss on marketable equity securities						(351)	(351)
Stock issued for acquisition of minority interest		295	153,794	3,124			3,419
Tax benefit from exercise of non-qualified stock options		604					604
Balance, December 29, 1979	28,038,187	$94,749	(426,660)	$(6,534)	$534,811	$(11,698)	$611,328
Net earnings for the year					94,386		94,386
Dividends on common stock, $1.40 per share					(38,768)		(38,768)
Exercise of stock options	89,680	903					903
Decrease in net unrealized loss on marketable equity securities						1,559	1,559
Stock contributed to employee stock ownership plan		417	56,259	862			1,279
Tax benefit from exercise of non-qualified stock options		355					355
Dividends reinvested under stock purchase plan	15,005	324					324
Balance, January 3, 1981	28,142,872	$96,748	(370,401)	$(5,672)	$590,429	$(10,139)	$671,366

The accompanying notes are an integral part of the consolidated financial statements.

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Consolidated Statement of Changes in Financial Position

Years Ended January 3, 1981, December 29, 1979 and December 30, 1978 (In thousands of dollars)

	1980 (53 Weeks)	1979 (52 Weeks)	1978 (52 Weeks)
Sources of Working Capital			
From operations:			
Net earnings	$ 94,386	$ 85,721	$ 84,596
Loss from operations to be discontinued	8,400		
Earnings from continuing operations	$102,786	$ 85,721	$ 84,596
Charges (credits) to earnings not involving funds:			
Depreciation and amortization	86,166	71,574	65,179
Provision for deferred federal income taxes	10,676	15,975	9,739
Tax benefit from operations to be discontinued	18,000		
Gain on sale of subsidiary			(3,441)
Loss on marketable investment securities	94		4,007
Total from operations	$217,722	$173,270	$160,080
Capital stock issued	1,227	1,952	1,237
Capital stock issued for acquisition		3,124	
Additions to long-term debt and obligations under capital leases	77,946	27,159	11,801
Proceeds from sale of marketable investment securities	3,504		7,488
Proceeds from sale of subsidiary			10,000
Net book value of fixed asset disposals	9,981	7,218	6,499
Total sources	$310,380	$212,723	$197,105
Uses of Working Capital			
Cash dividends paid to shareowners	$ 38,768	$ 34,524	$ 24,218
Capital expenditures	239,130	176,933	114,504
Increase in leased property under capital leases	15,596	3,996	11,801
Advances to operations to be discontinued	4,781	1,961	2,330
Reduction of unredeemed trading stamps			26,927
Reduction of long-term debt and obligations under capital leases	31,973	16,035	17,903
Deferred taxes due resulting from change to LIFO		16,811	
Employees' benefit fund payments, net of provision	928	1,875	3,145
Other changes, net	(89)	2,225	1,167
Total uses	$331,087	$254,360	$201,995
Net decrease in working capital	$ 20,707	$ 41,637	$ 4,890

Analysis of Working Capital Changes

	Increase (Decrease)		
Current asset changes:			
Cash and temporary cash investments	$ 17,638	$ (58,234)	$ (2,237)
Inventories	(5,430)	83,371	73,682
Other current assets	55,600	8,964	9,873
Net increase in current assets	$ 67,808	$ 34,101	$ 81,318
Current liability changes:			
Current portion of debt obligations	$ 1,287	$ 16,651	$ (3,525)
Accounts payable	37,036	50,908	72,597
Accrued expenses and taxes	50,192	8,179	44,063
Current portion of unredeemed trading stamps			(26,927)
Net increase in current liabilities	$ 88,515	$ 75,738	$ 86,208
Net decrease in working capital	$ 20,707	$ 41,637	$ 4,890

The accompanying notes are an integral part of the consolidated financial statements.

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All amounts are in thousands of dollars except per share amounts.

Accounting Policies

The following is a summary of the significant accounting policies followed in preparing the financial statements. These policies conform to generally accepted accounting principles and have been consistently applied except for the adoption of the LIFO method of inventory valuation in 1979.

Principles of Consolidation

The consolidated financial statements include the Company and all of its subsidiaries. Certain partially-owned affiliated companies are included in the financial statements on the equity basis. Certain amounts in the financial statements for prior years have been reclassified to conform to the 1980 presentation.

Marketable Investment Securities

Marketable investment securities consist of bonds, notes, and common and preferred stocks held for investment. Dividend and interest income are accrued as earned. The cost of marketable investment securities sold is determined on the specific identification method.

Marketable equity securities (common and preferred stocks) are carried at the lower of cost or market. A valuation allowance, representing the excess of cost over market of these equity securities, is included in shareowners' equity. Other marketable investment securities (bonds and notes) are carried at cost unless there is a permanent impairment of value at which time the securities are valued at market. In management's opinion there is no indication of a permanent loss in value of the portfolio and there is no present intention to liquidate the securities at less than cost.

Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation and amortization, which include the amortization of assets recorded under capital leases, are computed principally on the straight-line basis.

Building and land improvements are depreciated based on lives varying from ten to forty years and equipment based on lives varying from three to twenty years. Leasehold improvements are being amortized over their useful lives which generally approximate twelve and one-half years.

Excess of Cost of Investments in Consolidated Subsidiaries Over Equities in Net Assets

The excess of cost of investments in consolidated subsidiaries over equities in net assets at dates of acquisition originating prior to November, 1970 is not being amortized because, in the opinion of management, there has been no decrease in value. Amounts arising after October, 1970 are not significant and are being amortized on the straight-line basis over forty years.

Capitalization of Interest

Interest attributed to funds used to finance major capital expenditures is capitalized as an additional cost of the related assets. Capitalization of interest ceases when the related assets are substantially complete and ready for their intended use. The change to this policy was made in 1979 in accordance with Statement of Financial Accounting Standards No. 34 and had no material effect on net earnings or the overall financial statements.

Deferred Federal Income Taxes and Investment Tax Credits

Deferred federal income taxes include the amount of tax applicable to the excess of depreciation for tax purposes over depreciation used for financial reporting purposes less the amount of tax applicable to the unfunded pension liability and, in 1978, the amount of tax applicable to the change in 1973 from the LIFO (last-in, first-out) to the FIFO (first-in, first-out) method of inventory valuation.

Investment tax credits are included as reductions of income tax expense in the years in which the credits are used.

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Operations to be Discontinued

In 1980, the Company decided to dispose of its investments in the amusement park business. The Company and Taft Broadcasting Company (Taft) have been 50% joint-owners of Family Leisure Centers, Inc. (FLC), which operated the Carowinds and Kings Dominion amusement parks. A reorganization of FLC during 1980 resulted in the Company increasing its ownership to 81% from 50% and Taft becoming the sole owner of Carowinds. Subsequent to January 3, 1981, the Company agreed in principle to sell the Kings Dominion assets to Taft for one million shares of Taft Series B preferred stock with a par value of $20 per share with an estimated value of $17,800. The sale of the Kings Dominion assets will result in an estimated $18,000 tax benefit. The loss on operations to be discontinued, after deducting the anticipated tax benefits, has been provided to reflect the estimated net realizable value of the Company's investments in amusement parks.

Following the disposal of the Kings Dominion assets, the remaining investment in operations to be discontinued will be $6,728, representing the Company's 50% interest in the Hanna-Barbera's Marineland amusement park

The Company's share of net losses from amusement parks in 1980, 1979 and 1978 was $548, $436 and $102, respectively.

Accounting Change–Inventory

In 1979, the Company changed from the first-in, first-out (FIFO) method of valuing certain of its grocery inventories to the last-in, first-out (LIFO) method. The change in inventory valuation method was made to minimize inflation-induced inventory profits, to achieve a better matching of current costs with current revenues and to provide for greater comparability of the financial statements of the Company to those of other major companies in the supermarket industry.

The change to LIFO reduced net earnings in 1979 from $105,516 or $3.85 per share of common stock to $85,721 or $3.13 per share of common stock. Pro forma effects of retroactive application of LIFO are not determinable and there is no cumulative effect on accumulated earnings at December 30, 1978.

Marketable Investment Securities

Marketable investment securities include:

	1980	1979
Equity securities, at cost	$26,762	$30,360
Less valuation allowance charged against shareowners' equity .	(10,139)	(11,698)
Equity securities, at market ..	$16,623	$18,662
Bonds and notes, at cost......	853	853
	$17,476	$19,515

The portfolio of equity securities included gross unrealized gains and losses of $146 and $10,285, respectively at January 3, 1981. Net realized losses included in earnings amount to $94 in 1980, and $4,007 in 1978. There were no realized gains or losses on marketable investment securities in 1979. The valuation allowance charged against shareowners' equity decreased $2,920 during 1978 with $2,117 charged against earnings. The valuation allowance increased $351 during 1979, and decreased $1,559 during 1980, with $94 charged against earnings.

Inventories

Inventories at January 3, 1981 and December 29, 1979 include:

	1980	1979
Inventories, FIFO cost ...	$862,341	$817,355
Less LIFO reserve	(87,073)	(36,657)
	$775,268	$780,698

Inventories are stated at the lower of cost (principally LIFO) or market.

Approximately 68% of inventories at 1980 and 66% of inventories at 1979 were valued using the LIFO method. Cost for the balance of the inventories was determined by the FIFO method of inventory valuation. See note Accounting Change — Inventory.

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Earnings and earnings per share on a FIFO basis for the three years ending January 3, 1981 were:

	From Continuing Operations		Net	Net Earnings
	Earnings	Per Share	Earnings	Per Share
1980	$130,011	$4.70	$121,611	$4.39
1979	$105,516	$3.85	$105,516	$3.85
1978	$ 84,596	$3.11	$ 84,596	$3.11

Pension Plans

The Company has three noncontributory retirement plans for eligible employees, two of which have historically been funded. The third retirement plan, which was previously unfunded, is being funded over a period of forty years. The Company also contributes to multi-employer plans jointly administered by management and union representatives. The total pension expense for 1980, 1979 and 1978 was $85,587, $71,882 and $59,082, respectively. Past service costs of the Company's plans are amortized over forty years.

Accumulated plan benefits and plan net assets for the Company administered plans at January 1, 1980 were:

Actuarial present value of accumulated plan benefits:	
Vested	$193,120
Nonvested	6,455
	$199,575
Net assets available for benefits	$144,767

The weighted average assumed rate of return used in determining the actuarial present value of accumulated plan benefits was 6½%.

Information with respect to the actuarial present value of accumulated plan benefits and net assets available for benefits relating to the multi-employer plans was not determined.

Debt Obligations

Long-term debt as of January 3, 1981 and December 29, 1979 included:

	1980	1979
12⅜% sinking fund debentures maturing in 2005, with annual payments of $2,500 required from 1988 through 2004	$ 50,000	
9⅞% notes maturing in 1983	39,870	$ 50,000
9% sinking fund debentures maturing in 1995, with annual payments of $2,500 required from 1982 through 1995	30,390	32,122
8.7% sinking fund debentures maturing in 1998, with annual payments of $3,000 required from 1983 through 1998	47,784	50,949
8½% sinking fund debentures maturing in 2001, with annual payments of $2,500 required from 1983 through 2001	43,550	50,000
4½% to 9½% secured notes, annual payments due in varying amounts through 2004 (debt of real estate subsidiaries)	30,332	32,943
6⅜% to 9¾% industrial revenue bonds maturing in various years from 1983 through 2010	28,550	16,475
5.3% notes maturing in 1981 and a 15½% note which matured in 1980	3,750	4,600
	$274,226	$237,089
Less amount due within one year	(6,080)	(3,152)
	$268,146	$233,937

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The aggregate annual maturities and required payments of long-term debt for the five years subsequent to 1980 are:

1981	$ 6,080
1982	$ 2,437
1983	$50,695
1984	$ 8,770
1985	$10,315

Under certain of the loan agreements, payments of cash dividends are limited. Under the most limiting agreement, accumulated earnings were unrestricted in the amount of $142,000 at January 3, 1981.

Short-term borrowings of the Company averaged $8,907 and ranged up to $31,779 during 1980 at a weighted average annual interest cost of 13.9%. During 1979, short-term borrowings averaged $3,890 and ranged up to $41,975 at a weighted average annual interest cost of 14.6%. In 1978 there were no significant short-term borrowings.

At January 3, 1981, the Company had available a revolving credit aggregating $100,000, against which it may obtain interim loans until May 1, 1983. The interest rate on the interim loans would vary between the higher of 106% to 109% of the prime rate or the New York Composite 90 Day Certificate of Deposit Rate. At the Company's request, the interim loans may be converted into a term loan payable over four years. No amounts have been borrowed under this agreement.

The Company also had available lines of credit amounting to $30,600. The interest rate would be the prime rate at time of borrowing. These lines are subject to annual review by each bank.

Interest costs capitalized in 1980 and 1979 amounted to $1,327 and $942, respectively.

Leases

The Company operates principally in leased premises. Lease terms generally range from ten to twenty-five years with options of renewal for additional periods. Options provide in some cases for reduced rentals and/or the right to purchase. Certain of the leases provide for contingent rental based upon a percent of sales.

Rent expense (under operating leases) consists of:

	1980	1979	1978
Minimum rentals, net of minor sublease rentals	$118,404	$101,904	$ 91,065
Contingent rentals	12,228	10,623	8,720
Total	$130,632	$112,527	$ 99,785

Assets recorded under capital leases include:

	1980	1979
Distribution and manufacturing facilities	$ 97,213	$ 96,579
Store facilities	55,653	40,691
Less accumulated amortization	(41,486)	(36,884)
	$111,380	$100,386

Minimum annual rentals, net of subleased rentals which are minor in amount, for the five years subsequent to 1980 and in the aggregate are:

	Capital Leases	Operating Leases
1981	$ 16,013	$ 123,076
1982	15,988	119,427
1983	15,729	115,434
1984	15,318	112,511
1985	14,744	109,298
1986 and thereafter	221,779	1,152,310
	$299,571	$1,732,056
Less estimated executory costs included in capital leases	(13,792)	
Net minimum lease payments under capital leases	$285,779	
Less amount representing interest	(164,219)	
Present value of net minimum lease payments under capital leases	$121,560	

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Taxes Based On Income

The provision for taxes based on income consists of:

	1980	1979	1978
Federal			
Current	$34,211	$29,625	$47,616
Deferred	10,676	15,975	9,739
	$44,887	$45,600	$57,355
State and local			
Current	14,887	15,187	11,305
Total	$59,774	$60,787	$68,660

Investment tax credits reduced the tax provision by $18,217 in 1980, $12,717 in 1979 and $9,614 in 1978.

A reconciliation of the normal statutory federal rates and the effective rates is as follows:

	1980	1979	1978
Normal statutory rate ...	46.0%	46.0%	48.0%
State income taxes, net of federal tax benefit ...	4.9	5.6	3.8
Investment tax credits ..	(11.2)	(8.7)	(6.3)
Capital gains	(1.5)		
Other, net	(1.4)	(1.4)	(.7)
Effective rate	36.8%	41.5%	44.8%

Deferred federal income taxes included in the Consolidated Statement of Earnings consist of:

	1980	1979	1978
The tax effect of amounts expensed (included in earnings) for tax purposes in excess of amounts used for financial reporting:			
Depreciation	$11,785	$ 9,372	$6,623
Excess pension contribution	475	5,059	
Other	(1,584)	1,544	3,116
	$10,676	$15,975	$9,739

In 1973, the Company discontinued the LIFO method of valuing inventories and received Internal Revenue Service permission to spread the tax liability resulting from the change over a twenty year period. As a result of readopting the LIFO method of valuing inventories during 1979, deferred taxes, amounting to $16,811, became currently payable at December 29, 1979 in addition to the $29,625 reflected in the Consolidated Statement of Earnings.

Stock Option Plans

At January 3, 1981, options were outstanding to purchase 1,116,138 shares of common stock under the 1969 and 1976 Stock Option Plans (of which options on 748,952 shares were exercisable at that date) at prices ranging from $7.78 to $25.06 a share. Each option outstanding was granted at an option price equal to the fair market value of the stock at the date of grant. No further options may be granted under the 1969 Plan. Options may be granted under the 1976 Plan until 1986. At January 3, 1981, shares of common stock available for future options under the 1976 Plan amounted to 48,613 shares.

Changes during 1980 in options outstanding under the Stock Option Plans of the Company were:

	Shares Subject To Option	Option Price Range Per Share
Outstanding December 29, 1979	964,323	$ 7.78-$25.06
Granted	249,000	$16.63-$22.00
Exercised	(89,680)	$ 7.78-$17.94
Cancelled or expired	(7,505)	$12.85-$19.75
Outstanding January 3, 1981 ...	1,116,138	$ 7.78-$25.06

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The Company has made Stock Appreciation Rights (SAR's) available to certain officers. In general, the eligible optionees are permitted to surrender the related option and receive cash and shares of the Company's common stock having a value equal to the appreciation on the shares subject to the option. The appreciation of SAR's is charged to earnings based upon the market value of common stock. At January 3, 1981, rights related to options for 93,100 shares were outstanding and exercisable at prices ranging from $7.78 to $11.82 per share, expiring in 1981 and 1982.

Preferred Stock

The Company has authorized 750,000 shares of voting cumulative preferred stock which have a par value of $50 per share. None is outstanding at January 3, 1981.

Litigation

There are pending against the Company various claims and lawsuits arising in the normal course of business including, as of January 3, 1981, suits charging violations of certain antitrust and civil rights laws. Some of these suits purport or have been determined to be class actions and/or seek damages in very large amounts. Any damages that may be awarded in antitrust cases will be automatically trebled.

Sixteen antitrust suits alleging, among other things, price-fixing in the purchase and sale of meat, have been consolidated for pretrial and discovery purposes in the United States District Court in Dallas. On December 27, 1977, the Court entered a judgment dismissing nine of these suits which had been filed in 1975 and 1976. Appeals were filed in eight of the dismissed suits. The Fifth Circuit Court of Appeals reversed the dismissals and remanded the cases for further proceedings. No appeal was filed in the ninth suit, but a similar suit was filed in California under state antitrust statutes. That case was dismissed, and an appeal from such dismissal has been taken. The complaints in the remaining seven suits, which were filed in 1977, include certain allegations not contained in the earlier filed suits. Since discovery has been very limited, and since each of the suits, if tried at all, may go to a jury, the Company cannot predict their ultimate outcome. The Company believes, however, that it has substantial defenses available and should prevail in all.

Although the amount of liability at January 3, 1981 with respect to all claims and lawsuits cannot be ascertained, the Company is of the opinion that any resulting liability will not have a material effect upon the Company's financial position.

Segments of Business

The Company's segments of business information for 1980, 1979 and 1978 are included on page 18.

Changing Prices (Unaudited)

The Company's information regarding the impact of changing prices on a constant dollar and current cost basis is presented on pages 31, 32 and 33.

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Report of Independent Certified Public Accountants

To the Shareowners and Board of Directors
The Kroger Co.

We have examined the consolidated balance sheets of The Kroger Co. and Consolidated Subsidiary Companies as of January 3, 1981 and December 29, 1979, and the related consolidated statements of earnings, shareowners' equity and changes in financial position for the years ended January 3, 1981, December 29, 1979 and December 30, 1978. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the consolidated financial position of The Kroger Co. and Consolidated Subsidiary Companies at January 3, 1981 and December 29, 1979, and the consolidated results of their operations and changes in their financial position for the years ended January 3, 1981, December 29, 1979 and December 30, 1978, in conformity with generally accepted accounting principles applied on a consistent basis except for the change in 1979, with which we concur, in the method of valuing inventories as described in Notes to Consolidated Financial Statements.

Coopers & Lybrand
3800 Carew Tower
Cincinnati, Ohio 45202
February 20, 1981

Coopers & Lybrand

A copy of the Company's 1980 report to the Securities and Exchange Commission, Form 10-K, is available to shareowners on request by writing: Irle R. Hicks, Treasurer, The Kroger Co., 1014 Vine Street, Cincinnati, Ohio 45201.

The annual meeting of shareowners will be held at the Corbett Tower, Music Hall, 1243 Elm Street, Cincinnati, Ohio on May 15, 1981, at 10 a.m.

Transfer Agent and Registrar
The First National Bank of Cincinnati
First National Bank Center
Fifth and Walnut Streets
Cincinnati, Ohio 45201
Telephone: 513-632-4648

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Since 1973, the United States has experienced rapid inflation as contrasted to the relatively low level of inflation existing in prior years. Continued inflation over time distorts traditional accounting measurements of income and capital. In an effort to produce financial information that discloses the effects of inflation, the Financial Accounting Standards Board (FASB) issued Statement No. 33, Financial Reporting and Changing Prices, which requires companies to explain the effect of inflationary factors on their operations by adjusting historical financial information using two different methods. This information includes disclosures about the effects of changes in both general inflation (constant dollars) and specific prices (current cost).

The constant dollar method measures the effect of the general rate of inflation on the Company's earnings, by expressing certain historical cost amounts in units of the same purchasing power as measured by the Consumer Price Index for All Urban Consumers (CPI-U). This measure of general inflation encompasses a wide range of commodities and is not necessarily representative of the inflation effect upon our business. The current cost method attempts to reflect the changes in prices of the resources employed specifically in our operations. These methods involve the use of assumptions, approximations and estimates. The results should not be viewed as precise measurements of the effects of inflation.

Earnings derived under these methods includes adjustments to merchandise costs and depreciation and amortization expense for these inflationary factors. The effects of inflation, on merchandise costs, have been recognized in the historical financial statements, to some extent, due to the adoption of the LIFO method of inventory valuation in 1979.

The accompanying statement of earnings and five-year summary of selected financial data were prepared to reflect those inflationary factors due to increases in the historical costs of merchandise and depreciation and amortization and their related assets. Amounts prior to 1980, have been adjusted to average 1980 dollars by use of the CPI-U.

The restated net assets result in an indicated increase in shareowners' equity which was greater on a specific price basis than that of general inflation. The gain from decline in purchasing power of net amounts owed is primarily attributable to the debt which has been used to finance inventories and capital expenditures. During a period of inflation, holders of monetary assets suffer an unrealized loss of general purchasing power, while holders of monetary liabilities experience an unrealized gain.

Both the constant dollar method and the current cost method result in lower net income than reported in the primary financial statements. Taxation of earnings under present tax law reduces the amount of earnings available to support future business growth because these changing prices adjustments are not deductible for income tax purposes. The effects of the higher taxation of earnings are demonstrated in the effective tax rates shown on the supplementary income statement.

Inflation is one of our Country's most serious domestic problems as evidenced by the 13% rate of inflation in 1980. The U.S. government's influence on our environment affects all aspects of our business. Our ability to meet the challenges of the 1980's depends on the government's establishment of effective and consistent policies to control inflation, encourage capital formation and stabilize energy supplies.

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Consolidated Statement of Earnings from Continuing Operations Adjusted for Changing Prices

For the Year Ended January 3, 1981 (53 Weeks)
(In thousands of dollars)

	As Reported In The Primary Statements (Historical Costs)	Adjusted For General Inflation (Average 1980 Constant Dollars)	Adjusted For Changes In Specific Prices (1980 Current Costs)
Sales	$10,317,000	$10,317,000	$10,317,000
Costs and Expenses:			
Merchandise costs, including warehousing and transportation	$ 8,012,000	$ 8,047,000	$ 8,036,000
Operating, general and administrative expenses	1,901,000	1,901,000	1,901,000
Rent	130,000	130,000	130,000
Depreciation and amortization	86,000	112,000	130,000
Dividend and interest income	(11,000)	(11,000)	(11,000)
Interest expense, including interest on obligations under capital leases	36,000	36,000	36,000
Total	$10,154,000	$10,215,000	$10,222,000
Earnings from continuing operations before taxes based on income	$ 163,000	$ 102,000	$ 95,000
Taxes based on income	60,000	60,000	60,000
Earnings from continuing operations	$ 103,000	$ 42,000	$ 35,000
Effective tax rate-taxes based on income	36.8%	58.8%	63.2%
Gain from decline in purchasing power of net amounts owed		$ 114,000	$ 114,000
Increase in specific prices of inventories and property, plant and equipment			$ 286,000
Less effect of increase in general prices			249,000
Excess of increase in specific prices over increase in general prices			$ 37,000

At January 3, 1981 specific prices of inventories totaled $866,000 and specific prices of property, plant and equipment, net of accumulated depreciation totaled $1,467,000.

The adjustment to merchandise costs, including warehousing and transportation, in the supplemental income statements is less than one percent, which reflects the Company's use of the LIFO method of accounting for approximately 68% of its inventories. The difference results primarily from restating the remaining inventories to a current cost equivalent. The constant dollar merchandise cost adjustment is larger due to the higher rate of increase of the CPI-U for 1980 as compared with the Company's specific price indexes.

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Five-Year Comparison of Selected Financial Data Adjusted for Effects of Changing Prices

(thousands of average 1980 dollars, except per share figures)

		1980 (a)	1979	1978	1977	1976 (a)
Sales	$	10,317,000	10,250,000	9,887,000	9,175,000	8,950,000
Constant Dollar Data:						
Earnings from continuing operations	$	42,000	39,000	14,000	9,000	8,000
Earnings from continuing operations per share of common stock	$	1.50	1.41	.51	.33	.29
Net assets at year-end	$	1,173,000	1,083,000	974,000	928,000	889,000
Current Cost Data:						
Earnings from continuing operations	$	35,000	27,000(b)			
Earnings from continuing operations per share of common stock	$	1.25	1.00			
Net assets at year-end	$	1,284,000	1,151,000(b)			
Excess of increase in specific prices over increase in general prices	$	37,000	(10,000)(b)			
General Information:						
Gain from decline in purchasing power of net amounts owed	$	114,000	123,000	84,000	62,000	44,000
Dividends per share	$	1.40	1.43	1.12	1.03	1.00
Market price per share at year-end		20¾	20⅜	20⅝	18⅜	16⅞
Average consumer price index		246.8	217.4	195.4	181.5	170.5

(a) Fifty-three weeks

(b) 1979 merchandise costs, including warehousing and transportation, and depreciation and amortization expense stated in average 1980 dollars, were \$8,026,000 and \$135,000, respectively. At December 29, 1979, specific prices of inventories and property, plant and equipment, net of accumulated depreciation, stated in average 1980 dollars, totaled \$883,000 and \$1,229,000, respectively. The 1979 increase in specific prices of inventories and property, plant and equipment, and the effect of increase in general prices, stated in average 1980 dollars were \$244,000 and \$254,000, respectively.

Notes to Supplementary Data on Changing Prices

Accounting Policies

The supplementary data on changing prices is based upon the historical financial statements as reported in the primary financial statements adjusted for (1) general inflationary factors relating to property, plant, and equipment and inventories and (2) the changes in specific prices relating to these items.

Depreciation expense was calculated using the same methods and rates of depreciation as used in the historical financial statements.

Income tax expense has not been modified for any timing differences, allocations or adjustments that may result from applying the different methods in preparing the supplementary data.

No attempt has been made to calculate the benefit derived from additional realization of selling price increases necessitated by a higher level of cost of operations resulting from the application of the constant dollar or current cost adjustments to the original historical cost of property, plant, and equipment and inventories.

Constant Dollars

The supplementary data on a constant dollar basis is expressed in average for the year dollars and reflects adjustments that have occurred in the purchasing power of the dollar as measured by the CPI-U published by the Bureau of Labor Statistics. These amounts do not purport to represent appraised values or any other measure of current value.

Current Cost

The current cost of inventories, and merchandise costs, represents the cost of purchasing the goods at year-end prices for inventory and prices in effect at date of sale for merchandise costs. They are estimated based upon the latest prices and information of merchandise costs available as of January 3, 1981, and December 29, 1979. The amounts for 1979 have been adjusted to average 1980 dollars based on the CPI-U.

The current cost of property, plant, and equipment and the related depreciation expense are estimates of what the Company's existing assets would cost at the respective balance sheet dates. The amounts for 1979 have been adjusted to average 1980 dollars based on the CPI-U. Several methods, including indexation, direct pricing and application of square footage building and equipment costs based upon current merchandising and facility concepts, were used in estimating these amounts. These values represent the estimated current costs of existing assets and do not consider technological improvements and efficiencies associated with the normal replacement of productive capacity.

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Ten Year Summary

	1980	1979	1978	1977
Operations				
(thousands of dollars, except per share figures)				
Sales	$ 10,316,741	9,029,315	7,828,071	6,747,553
Costs and Expenses	$ 10,154,181	8,882,807	7,674,815	6,640,881
Earnings from Continuing Operations before Taxes Based on Income—LIFO	$ 162,560	146,508		
FIFO	$ 212,976	183,165	153,256	106,672
Taxes Based on Income—LIFO	$ 59,774	60,787		
FIFO	$ 82,965	77,649	68,660	46,649
Earnings from Continuing Operations—LIFO	$ 102,786	85,721		
FIFO	$ 130,011	105,516	84,596	60,023
Discontinued Operations	$ 8,400			
Net Earnings—LIFO	$ 94,386	85,721		
FIFO	$ 121,611	105,516	84,596	60,023
Dividends	$ 38,768	34,524	24,218	20,551
Per Share				
From Continuing Operations—LIFO	$ 3.71	3.13		
FIFO	$ 4.70	3.85	3.11	2.22
Discontinued Operations	$ .30			
Net Earnings—LIFO	$ 3.41	3.13		
FIFO	$ 4.39	3.85	3.11	2.22
Dividends	$ 1.40	1.26	.89	.76
Balance Sheet Statistics				
(thousands of dollars, except per share figures)				
Inventories	$ 775,268	780,698	697,327	623,645
Working Capital	$ 226,923	247,630	289,267	294,157
Property, Plant and Equipment, net	$ 884,617	725,220	621,292	570,989
Total Assets	$ 1,997,545	1,793,271	1,653,029	1,528,721
Long-Term Debt	$ 268,146	233,937	223,736	238,892
Shareowners' Equity	$ 671,366	611,328	554,507	489,972
Per Share of Common	$ 24.17	22.14	20.34	18.06
Other Statistics				
(thousands of dollars, except stock prices)				
Funds Provided from Operations	$ 217,722	173,270	160,080	130,750
Capital Expenditures	$ 239,130	176,933	114,504	96,417
Rent	$ 130,632	112,527	99,785	88,363
Interest Expense	$ 35,736	29,385	29,983	30,626
Common Stock Price Range	$ 14-23¾	17½-27	12¾-18½	11⅝-14⅜
Retail Facilities				
(areas in thousands of square feet)				
Food Stores				
Opened	118	88	104	98
Remodeled	49	91	58	35
Closed	107	56	90	83
Stores—End of Year	1,245	1,234	1,202	1,188
Total Area	34,529	32,460	30,673	28,642
Drug Stores				
Opened and Acquired	42	38	7	11
Closed	32	21	48	41
Stores—End of Year	514	504	487	528
Total Area	5,841	5,657	5,591	6,108

(a) 1976 and 1980 were fifty-three week years

(b) In 1972 the Family Center operations were discontinued resulting in an extraordinary loss of $5,341 or $.20 per share. There was a credit of $587 or $.02 per share resulting from a change in the method of applying an accounting principle.

(c) In 1971 the Wisconsin operations were discontinued resulting in an extraordinary loss of $4,056 or $.15 per share

(d) Amounts for 1973, 1972, and 1971 were not restated for a change in accounting for leases and for the consolidation of previously unconsolidated subsidiaries. Restatement would not have a material effect on the amounts reported.

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1976	1975	1974	1973	1972	1971
6,182,991	5,421,296	4,893,384	4,319,960	3,799,019	3,715,096
6,097,816	5,362,417	4,811,772	4,266,267	3,762,130	3,645,711
85,175	58,879	81,612	53,693	36,889	69,385
37,250	24,822	36,729	23,777	11,762	31,638
47,925	34,057	44,883	29,916	25,127	37,747
				4,754	4,056
47,925	34,057	44,883	29,916	20,373	33,691
18,577	18,298	18,088	17,461	17,406	17,370
1.78	1.26	1.66	1.11	.94	1.41
				.18	.15
1.78	1.26	1.66	1.11	.76	1.26
.69	.68	.67	.65	.65	.65
558,347	500,110	490,640	438,219	358,038	327,559
298,528	216,524	158,418	229,095	178,743	189,603
544,472	534,979	526,439	344,088	332,065	325,271
1,445,302	1,302,049	1,269,045	1,077,517	873,577	816,265
259,561	213,085	164,498	151,471	94,017	93,246
455,273	423,721	418,477	392,852	380,041	376,624
16.85	15.71	15.51	14.57	14.12	14.02
114,327	95,579	101,222	71,719	54,537	76,744
81,906	70,161	116,720	70,244	55,335	48,813
82,611	74,632	67,341	71,925	60,114	56,451
27,713	25,438	23,384	12,199	8,921	10,140
8⅞-12⅝	7⅞-12⅛	7⅛-12½	7½-12¼	9½-16⅞	13⅜-23
90	71	83	80	59	67
33	40	84	68	57	74
137	92	127	160	126	157
1,173	1,220	1,241	1,285	1,365	1,432
26,850	26,415	25,594	24,706	24,896	25,688
20	56	64	36	46	47
13	27	35	19	28	20
558	551	522	493	476	458
6,399	6,234	5,633	4,883	4,525	4,253

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President, Joseph E. Seagram & Sons, Inc.

Raymond B. Carey, Jr.
Chairman of the Board and President, American District Telegraph Company

Lyle Everingham
Chairman of the Board, President and Chief Executive Officer

James P. Herring
Former Chairman of the Board

Jackson C. Hinds
Chairman of the Board and Chief Executive Officer, Entex, Inc.

Patricia Shontz Longe
Economist and Professor, Business Administration, University of Michigan

T. Ballard Morton, Jr.
President, Orion Broadcasting, Inc.

Thomas H. O'Leary
President, Missouri Pacific Corporation

John D. Ong
Chairman, President and Chief Executive Officer, The B.F. Goodrich Company

W. George Pinnell
Executive Vice President, Indiana University

R. Nelson Shaw
Former Chairman, Mercantile Stores Company, Inc.

Edward D. Smith
Of Counsel to Hansell, Post, Brandon & Dorsey, Atlanta Attorneys

Morley P. Thompson
President, Baldwin-United Corporation

Russell L. Wagner
Chairman of the Board and Chief Executive Officer, NLT Corporation

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William J. Sinkula
Vice President

John L. Strubbe
Group Vice President

Charles L. Thomas
Group Vice President

Operating and Staff Vice Presidents

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Paul A. Gibson, *Personnel*
Don A. Hirsch, *Labor Relations*
Jack G. Hudson, *Controller*
Lorrence T. Kellar, *Capital Management*
C. Daniel Nash, *Tax Counsel*
Jack W. Partridge, Jr., *Public Affairs*

Kroger Food Stores

Headquarters Staff
R. Gus Bublitz, *Advertising*
Robert L. Cottrell, *Distribution Administration*
Bobbie L. Criswell, *Distribution Operations*
Donald F. Dufek, *Store Operation Services*
Donald M. Elliott, *General Merchandise Sales & Procurement*
Richard W. Goff, *Meat Plant Operations*
J. Wayne Harris, *Produce Merchandising*
Dean A. Hicks, *Marketing Administration*
James E. Hodge, *Real Estate*
George L. Irwin, *Delicatessens/Bakeries*
Thaddeus J. Kaczmarowski, *Facility Engineering*
Adrian L. Vannice, *Grocery Merchandising*

Marketing Areas
Richard L. Bere, *Columbus*
Newton W. Briggs, *Dallas*
David A. Burt, *Michigan*
Walter R. Dryden, *Southland*
Theodore Engel, *Central*
Robert G. Everingham, *Houston*
Joel E. Greenisen, *Louisville*
Robert L. Hayden, *Market Basket*
James A. LeRoy, *Delta*
Robert E. Saffron, *Cincinnati*
Nerville A. Sawall, *Gateway*
Richard D. Schill, *Carolinas*
Edwin A. Sieveking, *Mid-Atlantic*
Gerald L. Wolken, *Erie*

Kroger Manufacturing

Marshall H. Gooch, *Personnel*
George M. Laughlin, *Grocery Products Division*
William R. Pugh, *Baked Foods Division*
Ronald R. Rice, *Dairy Foods Division*
John W. Strohbach, *Engineering*
William Harold Wall, *Agri-Products*
Steven D. West, *Business Development & Marketing*
Robert M. Williams, *Research and Developmental Engineering*
Len L. Witt, *Procurement*

SupeRx Drug Stores

Headquarters Staff
Clyde N. Ballsrud, *Real Estate*
Frank Corella, *New Stores*
Robert L. Griffith, *Human Resources*
Albert G. Harsnett, *Advertising*
Gary E. Hendren, *Marketing*
Norbert J. Panko, *Controller*
Jerome L. Thole, *Operations*
Walter W. White, *Operating Services*

Retail Operations
Ronald R. Baumgarth, *North East Region*
Dennis O. Curran, *Florida Region*
Larry E. Slade, *North Central Region*

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